

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE EASTERN DISTRICT OF TENNESSEE

In re

PREMIER HOTEL DEVELOPMENT
GROUP d/b/a Hospitality
Consultants, The Carnegie
Hotel, Austin Spring Spa
& Salon, and Luigies;
PREMIER INVESTMENT GROUP
d/b/a Premier Investments;
and SAMUEL T. EASLEY,

Debtors.

Nos. 01-20923, 01-20940
and 01-20922
Jointly Administered
Chapter 11

PREMIER HOTEL DEVELOPMENT
GROUP and WAYNE WALLS,
Liquidating Trustee,

Plaintiffs,

vs.

FIRST TENNESSEE BANK, N.A.,

Defendant.

Adv. Pro. No. 02-2045

M E M O R A N D U M

APPEARANCES:

JAMES R. KELLEY, ESQ.
NEAL & HARWELL, PLC
One Nashville Place, Suite 2000
Nashville, Tennessee 37219

-and-

FRED M. LEONARD, ESQ.
27 Sixth Street
Bristol, Tennessee 37620
*Attorneys for Premier Hotel Development Group
and Wayne Walls, Liquidating Trustee*

RICHARD B. GOSSETT, ESQ.
BAKER, DONELSON, BEARMAN & CALDWELL
633 Chestnut Street, Suite 1800
Chattanooga, Tennessee 37450
Attorneys for First Tennessee Bank, N.A.

MARCIA PHILLIPS PARSONS
UNITED STATES BANKRUPTCY JUDGE

This adversary proceeding involves the proper interpretation of the confirmed chapter 11 plan in the underlying bankruptcy case with respect to payment of the claim of the Public Building Authority of the City of Johnson City, Tennessee ("PBA"). After consideration of all of the evidence presented at the trial in this matter on February 26, 2003, the court finds for the plaintiffs and will enter an order granting them a judgment against the defendant in the amount of \$100,000. This is a core proceeding. See 28 U.S.C. § 157(b)(2)(A) and (O).

I.

As set forth in the memorandum opinion filed in this proceeding on January 17, 2003, the plan of reorganization of debtor Premier Hotel Development Group ("PHDG") was confirmed on December 12, 2001. The plaintiffs in this action are PHDG and the liquidating trustee under the confirmed plan, Wayne Walls. The defendant is First Tennessee Bank, which held a lien on the debtor's principal asset, the Carnegie Hotel.

The complaint states that under PHDG's plan, the Carnegie Hotel was to be sold pursuant to a foreclosure sale under First Tennessee's deed of trust to an entity to be formed by Callen & Johnson Investments, LLC; that \$320,000 of the sale proceeds would be escrowed pending the determination of the priority claim of PBA; and that to the extent PBA's priority claim was reduced below \$320,000, 50% of the savings would go to the bankruptcy estate with the other 50% to First Tennessee. The plaintiffs alleged in their complaint that notwithstanding the anticipated sale to a Callen & Johnson entity, no such entity bid at the foreclosure sale. Instead, First Tennessee was the high bidder based on its credit bid of \$7 million, although within days of the foreclosure sale First Tennessee sold its interest in the hotel to Carnegie Hotel Investors, L.P., a Callen & Johnson entity, on December 28, 2001, for a gross sale price of \$7.64 million. The plaintiffs alleged that contrary to the confirmed plan, the sum of \$320,000 was not set aside from the sale proceeds for PBA's claim. Rather PBA was paid this amount at closing at First Tennessee's direction without resolution of the allowability of PBA's claim. The plaintiffs alleged that in authorizing this payment, First Tennessee violated the confirmed plan and deprived the debtor of its opportunity to challenge PBA's claim and potentially recover

one-half of \$320,000, i.e., \$160,000. Accordingly, the plaintiffs requested a judgment against First Tennessee in this amount.

First Tennessee responded that the confirmed plan only provided for the escrow of \$320,000 if the foreclosure sale price for the hotel exceeded the secured claims and that since this did not occur no escrow was required. First Tennessee also asserted that PHDG's own breach of the plan's directives necessitated the payment to PBA. Fee title to the hotel was actually held by PBA, although PHDG held a leasehold interest coupled with an irrevocable \$10 purchase option. Because First Tennessee's lien was only on PHDG's leasehold interest, the plan provided for PHDG to exercise its purchase option and then transfer fee title to the ultimate purchaser of the hotel. First Tennessee alleged that PHDG failed to exercise the purchase option and that as a result, fee title to the hotel had to be obtained directly from PBA, which refused to convey title absent immediate receipt of the \$320,000.

The parties cross moved for summary judgment on these issues, along with the question of whether PBA's claim, had it not been paid and remained a claim against the bankruptcy estate, would have been entitled to priority status. In a memorandum opinion filed January 17, 2003, the court concluded

that the confirmed plan "contemplated the escrow of \$320,000 from the foreclosure sale proceeds pending resolution of PBA's claim regardless of the amount of the sale proceeds." Nonetheless, the court was unable to grant plaintiffs' summary judgment motion because the record was insufficient to evaluate First Tennessee's contention that its failure to escrow the \$320,000 was necessitated by PHDG's own failure to exercise the purchase option. The court was also unable to resolve the issue of whether PBA's claim against PHDG would have been entitled to priority status although court did determine that the obligation was not a tax. Accordingly, both summary judgment motions were denied and this proceeding was set over for trial.

At trial, counsel for the parties announced that they had agreed that PBA's claim, had it remained a claim against the estate, would have been entitled to administrative expense status for \$120,000, such that one-half of the savings and thus the amount of any judgment in favor of the plaintiffs would be \$100,000. In addition, the parties stipulated, *inter alia*, to the following facts in their joint pretrial statement:

1. "PHDG constructed the [Carnegie] Hotel and operated the Hotel from its opening in March 2000 until its sale on December 28, 2001. The [PBA] owned the land upon which the Hotel was built. PHDG entered into a Lease Agreement on March 23, 2000,

with PBA for use of the land upon which the Hotel was built (the "Lease"). The Lease also granted PHDG an option to purchase the land."

2. "The PBA also owns the parking garage adjoining the Hotel ... [and] [o]n March 23, 2000, PHDG entered into the Parking Garage Management Agreement with the PBA (the "Parking Agreement")."

3. "PHDG was indebted to First Tennessee in the approximate amount of \$9.6 million. First Tennessee was the beneficiary of a duly executed and recorded first deed of trust on PHDG's leasehold interest in the Hotel."

4. "Under the Lease, rent was based on a 'Hypothetical Tax Amount' and was due on December 31 each year. The rent due ... was \$160,000 per year during the term of the Lease. No rent had been paid by the Debtors under the Lease [and] PBA had demanded payment of \$320,000 as a priority claim, representing the rent due since the inception of the Lease.... PHDG did not assume the Lease which was thereby rejected by PHDG."

5. The attorneys for First Tennessee and PHDG along with the principals of each met "on several occasions prior to and following the filing of the Debtors' bankruptcy cases in an attempt to work out the issues between the parties." These negotiations "resulted in a Plan Agreement dated ... October 5,

2001."

6. Following the negotiation of the Plan Agreement, ... [the debtors] filed a plan of reorganization. A series of amendments to the Plan ... were ... filed ... in response to various objections raised by creditors," resulting in confirmation on December 12, 2001, of the Third Modified Plan as amended by the Second Amendment to the Third Modified Plan.

7. "The foreclosure sale was conducted on December 18, 2001 as contemplated by and pursuant to the Plan. First Tennessee was the high bidder."

8. Thereafter, at a closing on December 28, 2001, PBA conveyed its title to the land on which the Hotel is located to Carnegie Hotel Investors, L.P. (the "Purchaser") and the trustee under First Tennessee's deed of trust similarly conveyed to the Purchaser PHDG's interest in the Hotel as obtained in the foreclosure. "The Purchaser did not assume the Parking Agreement with the PBA. The PBA refused to convey its interest in the land without payment of \$320,000 owed under the Lease.... PBA subsequently filed a pleading in the bankruptcy court withdrawing its claims."

9. "Upon application of all the proceeds paid to First Tennessee from the sale of the Hotel to the Purchaser, First Tennessee has a remaining balance owed it of approximately \$2.6

million by PHDG."

III.

First Tennessee's evidence and argument at trial revolved around two primary contentions. The first was that "[t]he Debtors failed to take reasonable action to resolve the claim of the PBA within time sufficient to allow an expeditious closing of the sale of the Hotel as required by the Plan, and Plaintiffs cannot recover damages from First Tennessee which were a result of such failure." The second is that "[t]he Plaintiffs cannot meet the burden of proof to show that damages were suffered as a proximate result of First Tennessee's failure to escrow \$320,000 from the sale proceeds rather than to pay those funds to the PBA since the sale would not have closed had the funds been withheld from the PBA, and there would have been no proceeds to escrow." In this regard, First Tennessee notes that even if PHDG had exercised its purchase option such that it would have had fee title to the Hotel and thus could have conveyed title to the ultimate purchaser, no sale would have taken place absent immediate payment to PBA because "PBA would not grant to the owners of the Hotel access to the Parking Garage unless all amounts owed PBA by the Debtors were paid in full."

First Tennessee's first assertion regarding PHDG's failure to timely to resolve PBA's claim is without merit. The confirmed plan plainly contemplated that the foreclosure sale would occur within days after confirmation and that resolution of PBA's claim would occur post-sale. In fact, the plan provides for the escrow of the sum sought by PBA out of the sale proceeds so that the dispute over PBA's claim would not delay the sale. As set forth in Paragraph (a) of Article V of the confirmed plan:

The Public Building Authority of the City of Johnson City has [sic] contending that it is entitled to a payment in lieu of taxes under the ground lease of the property on which the Carnegie Hotel is built of about \$320,000.00 for the years 2000 and 2001 and that such claim is entitled to Priority Claim status. Several creditors have objected to this Priority Claim status. The Debtors and the Authority have negotiated in an attempt to resolve this dispute but have not been successful. In order to effect the closing of the sale of the Carnegie Hotel, the Debtors will withhold from the sale proceeds the amount of the alleged Priority Claim of the Authority for payments in lieu of taxes approximately \$320,000.00. All rights of the Authority, including any lien rights, will attach to these escrowed funds. The Debtors and the Authority will retain their respective rights with respect to this amount and the Court will determine by subsequent proceedings the extent to which these funds should be paid to the Authority or the estate. In the event that the Authority is not entitled to payment of some or all of these funds, pursuant to the agreement between the Debtors and First Tennessee, one-half of such savings will go to the Debtors' estates and one-half will go to First Tennessee....

Neither PBA nor First Tennessee voiced any objection to this

provision. In fact, this language was set forth in the Third Modified Plan's Second Amendment filed December 12, 2001, and the parties have stipulated that at the confirmation hearing held on December 12, 2001, "First Tennessee ... affirmed its acceptance of the Amendment." Accordingly, any contention that PHDG breached the plan by not resolving PBA's claim prior to the post-confirmation sale is not supported by the confirmed plan.

The court next turns to First Tennessee's second argument which is premised on lack of proximate cause. First Tennessee argues that in order to prevail in this action, "[p]laintiffs are required to prove that, had First Tennessee escrowed the funds, the sale of the Hotel would have gone forward within the time contemplated by the Plan and that no moneys would have been due the PBA from the proceeds of the sale upon an adjudication of PBA's claim." First Tennessee maintains that PHDG cannot meet this burden of proof because no sale would have taken place unless the purchaser obtained a deed to the land, that PHDG could not convey the land because it had not exercised the purchase option, and that as a result, title had to be obtained from PBA which refused to convey title absent payment in full of the sum allegedly owed it by PHDG. Additionally, First Tennessee asserts that even if PHDG had been able to convey title to the land, the sale would not have occurred unless the

purchaser had access to the parking garage and PBA would not grant such access without payment in full. In a nutshell, First Tennessee's argument is that without payment to PBA, there would have been no closing, and thus no proceeds over which to fight.

As to the contention that the sale to Carnegie Hotel Investors, L.P. would not have closed absent a deed and an agreement regarding the parking garage and that PBA would agree to neither without payment in full, the evidence was not disputed. The parties stipulated that "PBA refused to convey its interest in the land without payment of \$320,000 owed under the Lease." D.R. Beeson, the real estate attorney who conducted the closing, testified that the deed from PBA would not have been given absent payment of the sum which PBA alleged it was owed by PHDG. Similarly, Ellen Buchanan, who is employed by the City of Johnson City as a special projects manager and a liaison to PBA, testified that PBA had to be made whole before any agreement regarding the parking garage would be entered into and that she was directed to communicate that position to all prospective buyers. Ms. Buchanan also testified that she delivered the deed from PBA to the closing and required that the monies be paid before the deed was delivered.

With respect to whether the PHDG itself breached the terms of the confirmed plan by not exercising its purchase option, the

evidence was not quite so clear. The plan does provide that "[o]n or before Confirmation, PHDG will exercise its \$10.00 purchase option and cause fee title to the Carnegie Hotel to be transferred to the purchaser at or after the foreclosure sale." Debtor Sam Easley, the majority general partner of debtor Premier Investment Group, the majority general partner of PHDG, testified that his attorney, Fred Leonard, told him in the summer of 2001 to exercise the option and that based on this directive, he took a check for \$10.00 and a letter to the City of Johnson City advising that PHDG was exercising its option. Mr. Easley testified that the check was cashed. Mr. Easley also stated that he instructed PHDG's attorney, Jim Kelley, to send a letter dated December 6, 2001, to the attorney for PBA, wherein Mr. Kelley stated:

To the extent that the earlier communications did not suffice, please consider this letter as a notice of intent to exercise the purchase option for the Carnegie Hotel property. It's my understanding that this will be considered at the meeting of the Authority to be held on the 17th. We contemplate that the closing will take place on the 18th.

I previously sent you a form of deed. I assume that the Authority would quit claim the property to [PHDG], which would then execute a deed to the purchaser, all consistent with the provisions of the Bankruptcy Plan.

...

Please also let me know if there are any other actions that need to be taken by the hotel or by the

purchaser with respect to either the acquisition of the fee or the assumption of the lease.

No evidence or testimony was offered as to whether the PBA responded to this letter or addressed PHDG's purchase option at its December 17 meeting. Whatever the result of the meeting, it is clear that PBA did not quitclaim the property to PHDG, but instead conveyed the property to the new purchaser at the closing.

Notwithstanding First Tennessee's claim of foul at this time for PHDG's failure to exercise its purchase option, there is no evidence that First Tennessee raised the issue either prior to or in connection with the closing. Mr. Easley testified that when a Callen & Johnson entity failed to bid on the hotel at the December 18, 2001 foreclosure sale, everyone, including himself, Messrs. Callen and Johnson, the attorneys for the parties, and two principals of First Tennessee, went to the offices of First Tennessee's attorney to discuss the matter. Mr. Easley testified that after a series of discussions in different rooms involving different individuals, it became apparent that he would have to withdraw from the deal which he stated that he agreed to do. Mr. Easley testified that he asked Ronald Willard, one of First Tennessee's officers, "who owns the hotel?" According to Mr. Easley, Mr. Willard responded that "you do and you will run it but we will do something before

December 31, 2001, because we don't want the hotel on our books at the end of the year." Mr. Easley testified that after that day, he heard nothing further until either Mr. Callen or Johnson telephoned him and advised that the "deal was done." Mr. Easley stated that no one requested that PHDG exercise its purchase option so that PHDG could convey the hotel to the new purchaser and that he was never informed that there was a problem obtaining a deed from PBA.

In light of this undisputed testimony, the court rejects First Tennessee's assertion that its failure to escrow the \$320,000 resulted from PHDG's failure to exercise its purchase option. If First Tennessee had been concerned about PHDG's inaction, it could have demanded at that time that PHDG comply with the plan and could have even filed an emergency motion with the court to force PHDG's compliance. The fact that First Tennessee did neither suggests that PHDG's omission was irrelevant. Presumably, First Tennessee's failure to make demand on PHDG was due to the fact that regardless of which entity conveyed the deed to the hotel, PBA still was a force to be reckoned with because of the parking garage. In any event, whatever the reason, PHDG's failure to exercise its purchase option does not provide a defense to First Tennessee in this proceeding.

Lastly, the court turns to the issue of the parking garage and whether the fact that PBA required immediate payment in full before it would enter into an parking garage agreement with Carnegie Hotel Investors, L.P. excuses First Tennessee's failure to escrow the \$320,000. In this regard, First Tennessee offered evidence that the Zoning Code of the City of Johnson City, Tennessee specified that hotels are required to have "one [parking] space per rental unit, plus one space for each two employees, plus one space per two hundred square feet of gross floor area devoted to eating or entertainment." The parking agreement that had been in effect between PHDG and PBA provided for the Hotel to have up to 172 spaces in the city's parking garage. Ms. Buchanan testified that the hotel does not have sufficient parking unless the parking garage was utilized because the hotel itself has only 12 spaces while the restaurant located within the hotel has 75-80 parking spaces. Ms. Buchanan also testified that the only way the City of Johnson City would allow use of a site was if there was sufficient parking on site or if there was a legal or contractual arrangement for another site.

The evidence offered in this case must considered in the context of the terms of the confirmed chapter 11 plan because "a confirmed Chapter 11 plan is essentially a new contract between

a debtor and its creditors." *Eagle-Picher Indus., Inc., v. Caradon Doors and Windows, Inc., (In re Eagle-Picher Indus., Inc.)*, 278 B.R. 437, 451 (Bankr. S.D. Ohio 2002). "As with any contract, the starting point for review of a plan is its plain language." *Charter Asset Corp. v. Victory Markets, Inc. (In re Victory Markets, Inc.)*, 221 B.R. 298, 303 (B.A.P. 2nd Cir. 1998).

Notwithstanding First Tennessee's assertion that prior payment to PBA was necessary in order to effectuate the sale of the hotel, the plan itself does not address the parking garage. The terms of the plan were negotiated by the debtor and First Tennessee and incorporated in a plan agreement dated October 5, 2001, wherein the debtor agreed to file a plan of reorganization providing for the sale of the Hotel pursuant to a foreclosure sale conducted by First Tennessee. The plan agreement set forth detailed instructions as to how the proceeds from the sale would be distributed, with the distribution schemes varying based on the amount of the proceeds. For example, if the proceeds were equal to or more than \$8.5 million, \$255,000 of the proceeds would go to the debtor for payment of administrative expenses. As this court concluded in its January 17, 2003 memorandum opinion, each distribution scheme, regardless of the amount of the proceeds, provided for PHDG and First Tennessee to split the

savings equally if PBA's \$320,000 claim were reduced. The plan agreement also provided that in the event a confirmation order was not entered by December 17, 2001, First Tennessee would have relief from the automatic stay to foreclose and would retain all of the sale proceeds. Mr. Easley testified that First Tennessee had wanted the deal done and off its books by the end of the year, December 31, 2001. All of these provisions were incorporated into the plan of reorganization filed by the debtor and confirmed by the court.

Thus, PHDG's obligation under its agreement with First Tennessee was to obtain confirmation of a plan, which contained the agreed-upon terms, by December 17, 2001. If PHDG did so, it would at a minimum be entitled to one-half of the savings resulting from any reduction in PBA's claim. Clearly, PHDG kept its end of the bargain, it filed a plan containing the required provisions and this plan was confirmed on December 12, 2001, before the December 17 deadline. Correspondingly, First Tennessee was required to distribute the sale proceeds in accordance with the terms of the plan and as such was obligated to escrow the amount due PBA pending resolution of its claim by the court.

The fact that PBA required payment in full of the amount allegedly owed by PHDG before it would enter into a parking

agreement with a purchaser of the Hotel does not alter First Tennessee's obligations under the plan. First Tennessee chose to pay these sums so that a sale of the Hotel could be accomplished before the end of the year, even though the plan did not require that a sale be accomplished by any certain date.

Furthermore, in light of the Hotel's limited on-site parking space, it was foreseeable that any purchaser of the Hotel would have to make arrangements with PBA for access to additional parking. Presumably, in order to ensure that parking in the garage would be continue to be available, First Tennessee could have requested that the plan provide for the assumption and assignment of that agreement. Apparently, First Tennessee did not do so. There is no requirement in the plan that PHDG assume the parking garage lease and provide for its assignment to a new purchaser. Mr. Easley testified that in all of his discussions with First Tennessee, he was never asked to include in the plan anything about the parking garage.

The bottom line is that First Tennessee agreed in the plan to give the debtor the opportunity to contest PBA's claim and recoup one-half of any savings. Having agreed, First Tennessee may not deprive the debtor of that opportunity simply to satisfy its own timetable when PBA's ace in the sleeve in the form of the parking garage was foreseeable and avoidable. Accordingly,

an order will be entered contemporaneously with the filing of this memorandum opinion, granting the plaintiffs a judgment against First Tennessee in the amount of \$100,000.

FILED: May 5, 2003

BY THE COURT

MARCIA PHILLIPS PARSONS
UNITED STATES BANKRUPTCY JUDGE